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Economic Intelligence Weekly

Secret

CIA No. 8222/74
2 October 1974

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ECONOMIC INTELLIGENCE WEEKLY

2 October 1974

AGRICULTURE

World Grain Supplies Tighten; The 1974/75 world grain situation has perceptibly worsened in recent weeks, with lower production, stocks, and exports in prospect. [redacted] (See page 1.)

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India: Further Grain Problems; One of the countries hardest hit by worldwide grain shortages, India must seek additional supplies in the aftermath of a poor summer monsoon. [redacted] (See page 2.)

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Eastern Europe: Grain Crop Smaller; With the harvest almost over, we estimate grain production in Eastern Europe at 72 million tons, about 1-1/2 million tons below the 1973 record. [redacted] (See page 3.)

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[redacted]

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INDUSTRIAL NATIONS

France Grapples With Inflation, Trade Deficit; Giscard now seems prepared to pay a higher cost in lost output to bring inflation and the trade deficit under control. [redacted] (See page 5.)

25X1

Italy: Labor Threatens Austerity Program; Key unions are pressing demands that would scuttle recently adopted anti-inflationary measures. [redacted] (See page 6.)

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The Bank of England has eased its tight monetary policy because of slackening economic activity and a spreading cash squeeze on corporations. Following six months of restricted growth, the money supply increased about 4% in the past two months. [redacted]

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Belgium continues to reject the use of tight fiscal policies to fight inflation, relying instead on monetary policy as the main weapon. Under the 1975 budget, ordinary expenditures will be up about 30%. Despite well-publicized tax increases, the budget deficit will be up sharply. [redacted]

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Australia and New Zealand last week devalued their currencies by 12% and 9%, respectively. Canberra's devaluation is aimed at holding down imports, which contributed in part to the $1 billion balance-of-payments deficit registered during the year that ended in June. New Zealand has seen its official foreign exchange reserves drop to about $675 million at the end of August because of rapidly rising imports and weakening foreign demand for its exports. [redacted]

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INTERNATIONAL MARKETS

The Dollar declined against major European currencies last week but strengthened more than 1% against the yen. The sharpest declines were against the French and Swiss francs, both of which gained more than 1%. Paris' announcement last week of plans to limit oil imports was undoubtedly a factor in the strength of the franc. [redacted]

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Gold was fixed at $155.75 per ounce in London yesterday afternoon, up $8.25 for the week. Traders attributed its strength to political uncertainties in Portugal which might lead indirectly to problems for South Africa. [redacted]

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Copper Prices on the LME rose to 68 cents a pound on Monday, a gain of 3.6 cents for the week, on reports that Japanese copper sales on the LME would be cut back. Zinc prices recovered close to early September levels while lead prices remained steady. [redacted] (See Metals Price Chart, page A-3.)

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Reports of Frost Damage sent corn and soybean prices to 1974 highs and boosted wheat prices to late March levels. Sugar prices recovered from a slight downturn in mid-September to approach record levels again. Cotton prices continued their downward trek. [redacted] (See Agricultural Prices Chart, page A-4.)

COMMUNIST COUNTRIES

The Soviet Image of the US Economy; Data from the key Soviet statistical handbook show that the Kremlin has a fairly realistic picture of US economic strength. [redacted] (see page 7.)

Lower US-China Trade Projection; Rescheduling and cancellation of contracts has sharply reduced expected shipments of US agricultural products for the fourth quarter. [redacted] (See page 8.)

PUBLICATIONS OF INTEREST

[redacted]

Upsurge of Bilateral Economic Aid to the Less Developed Countries, First Half 1974 (See page 8.)

COMPARATIVE INDICATORS

Recent Data Concerning Internal Economic Activities (See page A-1.)

Recent Data Concerning External Economic Activities (see page A-2.)

Metal Prices (See page A-3.)

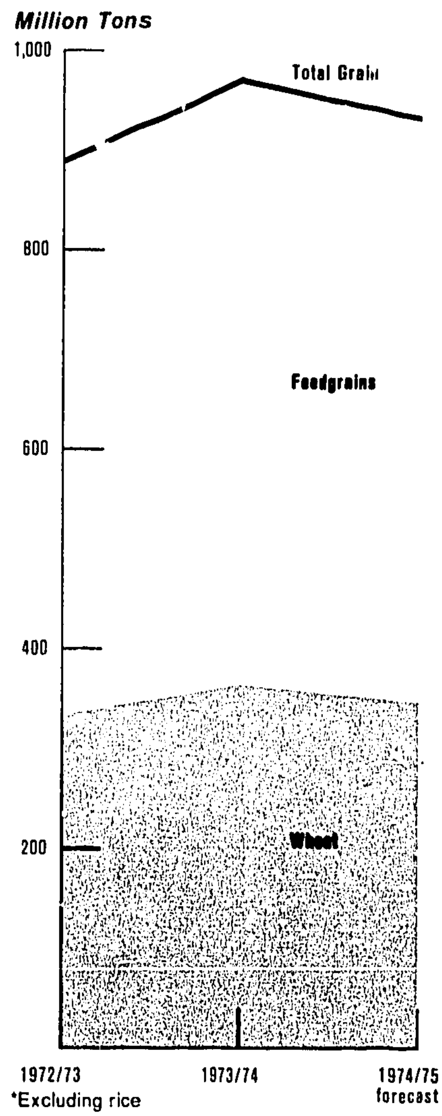
Agricultural Prices (See page A-4.)

Articles

WORLD GRAIN SUPPLIES TIGHTEN

The 1974/75 world grain situation has tightened further in recent weeks. We now forecast a 4% decline in grain production (excluding rice) from last year's record level of 969 million tons; last spring, chances seemed good that output would rise. Supplies of wheat and corn available for export in FY 1975 are expected to be down by 2% and 20%, respectively, even though stocks will be drawn down to record lows by 30 June 1975.

World Grain Production*



*Excluding rice

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Wheat

World wheat production is estimated to fall about 20 million tons, or 5% in 1974/75. While Argentina and Australia will export more wheat, the United States and the EC will export less because of reduced availability in the United States and increased use of wheat to feed livestock in the EC. Canada, with stocks equivalent to two years' domestic consumption, may have difficulty moving as much grain as last year because of transport strikes. With exportable supplies at 59 million tons and world import demand forecast at 61 million tons, stocks will be further drawn down and prices will remain high.

We estimate export demand for US wheat and flour at 28 million tons, compared with 31 million tons last year. This level of exports would place carryover stocks on 30 June 1975 at a record low of 6 million tons, only slightly more than needed for orderly marketing.

Note: Comments and queries regarding the ***Economic Intelligency Weekly*** are welcomed.

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Feedgrains

The supply situation for feedgrains, especially corn, is even tighter than for wheat. Production of corn in the major exporting countries is expected to be down by 11% to 149 million tons in 1974/75. US production is expected to decline to 127 million tons, or 40 million tons less than last year. This total may be trimmed further by damage from early frost. Production of corn by Argentina, South Africa, and Thailand probably will drop almost 7% to 22 million tons. Because stocks are the lowest in 20 years, corn available for export in FY 1975 will fall 9 million tons below last year to 34 million tons. Although import demand will also be down because of (a) high prices, (b) depressed livestock markets, and (c) increased feeding of wheat to livestock, the net effect will be additional upward pressure on prices and a further dwindling of stocks.

Export demand for US corn is forecast at 23 million tons, compared with 35 million tons last year. Even this reduced level of exports would draw down stocks 5 million tons by 30 June 1975 and by an additional 1.75 million tons through the end of the marketing year, 30 September 1975. This would leave a supply equal to no more than one month's domestic consumption.

Continuing Uncertainties

Major elements to be watched in the world grain market include:

- the impact of tight feedgrain supplies on the use of wheat in livestock feeding;
- the degree to which depressed livestock markets will decrease the demand for feedgrains;
- the effect of the size and quality of Soviet grain stocks and high world prices on Moscow's policy toward grain imports;
- the seriousness of transport problems in Canada, South Africa, and Argentina;
- the stockpiling policies of Middle East countries; and
- the extent of frost damage to grain production in North America.

[redacted] 25X1

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INDIA: FURTHER GRAIN PROBLEMS

India again faces a bleak grain situation due to a poor summer monsoon.

The major fall grain harvest is currently projected by the US embassy at 58 million to 62 million tons -- below last year's 67 million tons and close to the drought-reduced 1972 harvest of 57 million tons. India is worse off than in 1972 because:

- government stocks on 1 July were only 4 million tons, compared with 9 million tons on 1 July 1972, and
- the population has grown by 26 million.

In FY 1975, the government will be hard put to get the minimum 12 million tons needed for the state grain distribution system, which markets subsidized grain in urban and destitute rural areas. New Delhi can get only half this amount from stocks and the fall harvest. The other 6 million tons must be imported. To date, India has arranged for only 3 million tons:

- 1.8 million tons of wheat purchased from the United States,
- 430,000 tons of sorghum and 250,000 tons of wheat purchased from Argentina,
- 300,000 tons of wheat purchased from Australia and 40,000 tons obtained as a grant,
- 80,000 tons of wheat purchased from Canada and 140,000 tons obtained as a grant, and
- 100,000 tons of Soviet wheat carried over from last year's grain loan.

As for further supplies, New Delhi has requested 1 million tons of EC wheat -- one-half as grant, one-half as purchases -- which according to press reports will be arranged. India is also seeking another Soviet grain deal; Moscow appears unwilling to make any commitment until its own situation is clearer. Last week the Indian embassy in Washington confidentially requested PL-480 grain shipments. New Delhi remains loath, however, to request grain publicly. [redacted] 25X1

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EASTERN EUROPE: SMALLER GRAIN CROP

With the harvest practically over, we estimate grain production in Eastern Europe at 72 million tons, about 1-1/2 million tons below the 1973 record.

Because of the decline, East European grain imports are projected at 9 million tons in FY 1975, compared with 8 million tons in FY 1974. The USSR will supply about half, mostly wheat. The East Europeans will look to the United States for 2.0 million to 2.5 million tons of grain, predominantly corn, and to other Western sources for the balance.

Eastern Europe: Grain Production and Imports

Million Tons

	Production			Gross Imports	
	CY 1972	CY 1973	Estimated CY 1974	Preliminary FY 1974	Projected FY 1975
Total	**73.2**	**73.4**	**72.0**	**8.1**	**8.7**
Northern countries	37.6	40.2	39.2	7.8	8.2
Czechoslovakia	8.7	9.8	10.0	1.4	1.5
East Germany	8.5	8.5	8.7	3.4	3.5
Poland	20.4	21.9	20.5	3.0	3.2
Southern countries	35.6	33.2	32.8	0.3	0.5
Bulgaria	8.1	8.2	8.0	....	....
Hungary	10.6	11.4	11.6	0.1	0.1
Romania	16.9	13.6	13.2	0.2	0.4

Among the northern countries, East Germany and Czechoslovakia harvested record grain crops. Poland's crop, usually about 30% of the East European total, narrowly skirted disaster throughout the growing season. Nevertheless, the harvest of 20.5 million tons was only 6% below the 1973 record. Of the southern countries, Hungary had another bumper harvest, Bulgaria a slightly reduced crop, and Romania its second poor harvest in a row. Bucharest last week asked Washington for an additional $19 million in CCC grain credits for FY 1975, over and above the $31 million already arranged.

Exports of grain from the southern countries will top last year's total. Hungary expects its grain exports to approach 2 million tons, enough to finance a large part of its purchases of Western equipment. Romanian exports, mostly wheat, will probably not exceed the 700,000 tons sold in FY 1974. Bulgaria will be able to export about 300,000 tons of wheat, almost all to Middle Eastern and African customers.

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FRANCE GRAPPLES WITH INFLATION, TRADE DEFICIT

The recent steps taken by Paris to slow inflation and reduce the trade deficit reflect a new appreciation of the intractability of these problems. Giscard now seems prepared to pay a slightly higher price in lost output and employment to bring them under control. Nonetheless, he doubtless is unwilling to let economic growth slip much below the 4% mark from the 5.2% rate of the first half of 1974. The government remains intent on establishing its populist credentials and, above all, avoiding a recurrence of the 1968 riots that shook the country.

The government has been disappointed by lack of progress on the inflation and trade fronts since June, when it launched a program to dampen domestic demand. Rather than decelerating as hoped, inflation has remained at 15% – largely because of rising wage costs. Continuing monthly trade deficits of about $400 million suggest that trade cannot be balanced by yearend 1975 as planned.

In general, the new measures bear down on business while partially protecting the livelihood of lower income groups. The government is:

- pressing firms to cut prices of selected consumer goods by 5% and is restricting their freedom to pass on cost increases, while retaining only voluntary restraints on wages;

- readying a special tax on corporate excess earnings, in addition to the tax increases levied in June;

- limiting credit expansion in any 12-month period to 12%, down slightly from the rate established last spring; and

- planning to cut the volume of oil imports about 10% by broadening oil rationing to include industrial as well as household fuel supplies and by encouraging coal production.

These measures probably will bring the inflation rate down to 13% or so by yearend, in spite of exemptions from the credit restraints and some flouting of price controls. Restrictions on oil imports should trim the 1975 trade deficit by $1 billion. Discouragement of private investment will free additional capital goods for export. At the same time, the stimulus given to consumer demand by rising wages will keep the economic growth rate tolerably high. 25X1

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ITALY: LABOR THREATENS AUSTERITY PROGRAM

The federation that speaks for the three major union groups has proposed measures that would scuttle Rome's new austerity program, as follows:

- sweetening of cost-of-living clauses in wage contracts, including a retroactive lump-sum payment of $30 to each worker;
- linking of private pension payments of less than $150 a month to wage increases;
- raising public investment outlays, especially in the south; and
- rescinding of recent increases in electric bills and bus fares.

These demands presumably represent an opening position subject to negotiation with government and management. Labor is far from united on the proposals; several conservative leaders of the Christian Democratic union group have resigned in protest from the federation's executive committee.

Even partial implementation of the demands would dampen prospects for slowing inflation, curbing imports, and decreasing capital outflows. The wage increases alone would total between $1 billion and $1.5 billion – about one-fourth of the sum the government hopes to drain from households through its recent fiscal measures. Adoption of the whole package would essentially offset the contractionary impact of the fiscal program.

The federation's proposals are timed to coincide with an improvement in the Italian balance of payments, due partly to seasonal factors. A $395 million payments surplus in the 10 weeks ending 15 September reduced the deficit so far this year to $6.3 billion. Increased foreign financing of Italian imports since the imposition of the import deposit scheme in May 1974 has contributed to the recent surplus. Tight credit, high domestic interest rates, and slightly increased confidence engendered by the austerity program also helped by discouraging capital outflows and encouraging repatriation of capital from abroad. [redacted] 25X1

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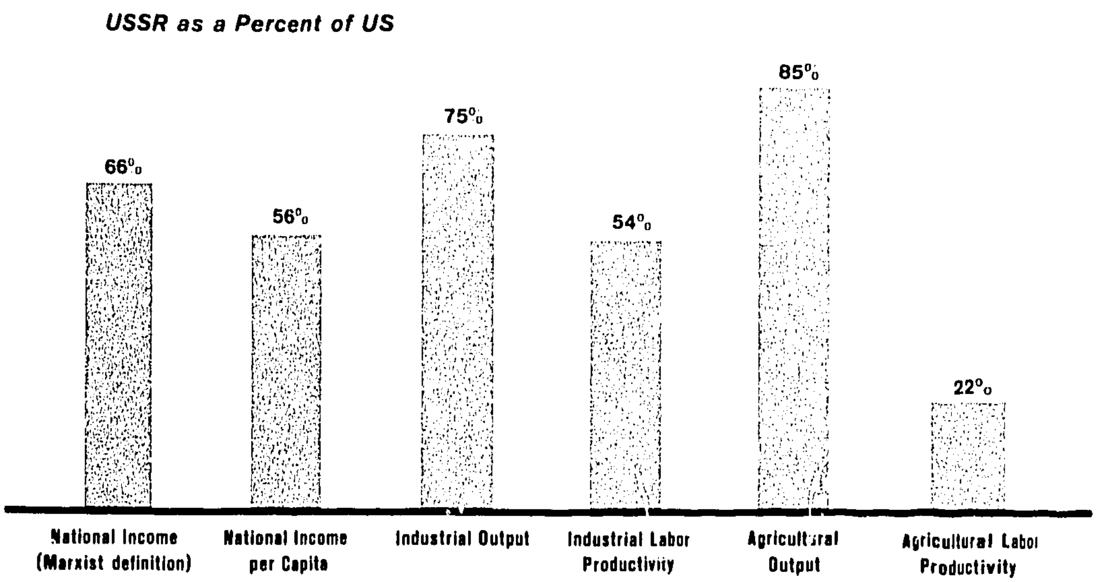
THE SOVIET IMAGE OF THE US ECONOMY

This chart, which uses data from the official Soviet statistical handbook, *Narodnoye khozyaystvo 1972*, shows that the Kremlin leadership has a fairly realistic picture of the comparative economic strength of the United States and the USSR.*

A Soviet Comparison of the Two Economies, 1972



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CIA estimates of these comparisons are less favorable to the USSR, to wit: GNP, 53%; per capita GNP, 45%; industrial output, 67%; industrial labor productivity, 39%; agricultural output, 76%; and agricultural labor productivity, 9%. The differences in percentages are attributable largely to variations in statistical concepts and methods.

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* The chart appeared in a recent CIA/OPR publication, *The Soviet Image of the US*, 11 September 1974,

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Notes

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[redacted] 25X1

Lower US-China Trade Projection

A sharp drop in the deliveries of agricultural products scheduled for the fourth quarter has led us to reduce our projection of US exports to China for the year, from $1.1 billion to about $800 million. Recent rescheduling or cancellation of contracts caused the drop. Three contracts covering 1974 delivery of about 1 million tons of wheat have been deferred until 1975. A large contract for US soybeans has been canceled because the Chinese discovered poisonous seeds in previous shipments. US exports to China of $709 million through August 1974 have already surpassed the $689 million total for 1973. Chinese exports to the United States are expected to reach $100 million, up from $64 million last year. [redacted] 25X1

Publications of Interest*

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[redacted]

Upsurge of Bilateral Economic Aid to the Less Developed Countries, First Half 1974
(ER RP 74-19, September, [redacted] 25X1

Members of OPEC were responsible for the large increase in undertakings that resulted in the $13.3 billion record pledges of bilateral official economic aid in the first half of 1974.

[redacted] 25X1

INTERNAL ECONOMIC INDICATORS

GNP*

Constant Market Prices

	Latest Quarter	Percent Change from Previous Quarter	Average Annual Growth Rate Since 1970	1 Year Earlier	Previous Quarter
United States	74 II	-0.4	3.6	-1.2	-1.6
Japan	74 II	0.6	5.7	-3.3	2.4
West Germany	74 I	1.2	3.5	1.5	5.0
France	73 IV	1.8	5.8	5.7	7.3
United Kingdom	74 I	-3.5	1.9	-4.4	-13.3
Italy	73 IV	1.9	3.7	5.3	7.7
Canada	74 I	1.7	5.4	3.0	7.0

WHOLESALE PRICES

Industrial

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Aug 74	2.4	9.8	27.5	32.9
Japan	Aug 74	1.0	11.3	32.8	14.9
West Germany	Jun 74	0.2	7.0	13.1	10.3
France	Aug 74	-0.7	12.4	30.3	-2.5
United Kingdom	Aug 74	1.3	11.3	25.3	19.3
Italy	May 74	0.7	14.5	48.3	44.1
Canada	Jun 74	0.1	10.9	23.5	16.1

INDUSTRIAL PRODUCTION*

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier**
United States	Aug 74	-0.4	4.0	-1.0	1.3
Japan	Jul 74	0.4	[illegible]	-1.4	-6.3
West Germany	Jun 74	-2.8	[illegible]	-1.1	-2.2
France	Jun 74	0.8	6.2	5.0	2.2
United Kingdom	Jun 74	0.6	2.3	-2.0	16.2
Italy	Jul 74	-2.5	5.0	4.2	1.6
Canada	Jun 74	0.6	6.2	3.3	-2.9

CONSUMER PRICES

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Aug 74	1.3	6.4	11.2	13.2
Japan	Aug 74	1.0	11.5	25.4	15.4
West Germany	Aug 74	0	6.1	6.9	2.5
France	Aug 74	0.8	8.2	14.5	13.4
United Kingdom	Jul 74	0.9	10.6	17.1	14.0
Italy	Aug 74	2.1	10.3	20.5	25.6
Canada	Aug 74	1.0	6.7	10.8	12.7

RETAIL SALES*

Current Prices

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier**
United States	Aug 74	0.6	10.1	9.9	13.7
Japan	May 74	4.7	13.0	15.9	-1.7
West Germany	Jun 74	-0.5	7.7	2.0	-0.1
France	May 74	6.2	8.5	18.1	1.3
United Kingdom	Jun 74	3.3	11.9	14.7	8.3
Italy	Apr 74	1.3	17.5	27.3	34.0
Canada	Jun 74	0.2	12.2	17.8	18.4

MONEY SUPPLY*

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier**
United States	Aug 74	0.3	5.9	5.4	3.4
Japan	Jun 74	1.6	17.9	15.7	17.6
West Germany	Jun 74	2.0	9.2	5.3	10.4
France	Jun 74	1.3	12.7	10.7	15.6
United Kingdom	Aug 74	1.2	8.8	0.6	3.5
Italy	Jan 74	0.1	20.7	22.7	22.5
Canada	Jul 74	0	12.7	9.6	12.5

MONEY-MARKET RATES

	Representative Rates	Latest Date	Percent Rate of Interest	1 Year Earlier	3 Months Earlier	1 Month Earlier
United States	Dealer-placed finance paper	Sep 25	10.93	8.75	9.00	12.00
Japan	Call money	Sep 18	13.00	8.75	12.63	13.75
West Germany	Interbank loans (3 Months)	Sep 25	9.40	13.84	9.60	9.50
France	Call money	Sep 18	13.50	10.75	14.50	13.75
United Kingdom	Sterling interbank loan (3 mo)	Sep 25	11.77	13.13	13.27	12.64
Canada	Finance paper	Sep 25	11.19	8.75	11.00	11.78
Euro-Dollars	Three-month deposits	Sep 25	11.60	10.80	13.41	13.91

***Seasonally adjusted.**
****Average for latest 3 months compared with average for previous 3 months.**

2 October 1974
Office of Economic Research/CIA

Note: US data provided by US government agencies

EXTERNAL ECONOMIC INDICATORS

EXPORTS*
f.o.b.

	Latest Month		Cumulative		
		Million US $	Million US $ 1974	1973	Percent Change
United States	Aug 74	8,370	63,285	44,014	43.8
Japan	Aug 74	4,865	34,305	22,647	51.7
West Germany	Aug 74	7,907	58,605	42,466	38.0
France	Aug 74	4,044	30,297	23,434	29.3
United Kingdom	Aug 74	3,237	23,403	18,618	25.7
Italy	Jun 74	2,270	13,285	9,401	41.3
Canada	Jul 74	2,753	18,292	14,287	28.0

IMPORTS*
f.o.b.

	Latest Month		Cumulative		
		Million US $	Million US $ 1974	1973	Percent Change
United States	Aug 74	9,502	65,408	44,870	45.8
Japan	Aug 74	4,474	35,396	19,926	77.6
West Germany	Aug 74	6,067	42,419	32,617	30.1
France	Aug 74	4,489	33,157	22,621	46.6
United Kingdom	Aug 74	3,986	31,469	21,385	47.2
Italy	Jun 74	2,827	16,852	10,708	57.4
Canada	Jul 74	2,778	17,711	13,056	35.7

TRADE BALANCE*
f.o.b./f.o.b.

	Latest Month		Cumulative (Million US $)		
		Million US $	1974	1973	Change
United States	Aug 74	-1,132	-2,123	-856	-1,267
Japan	Aug 74	391	-1,031	2,721	-3,752
West Germany	Aug 74	1,840	16,185	9,849	6,336
France	Aug 74	-445	-2,859	813	-3,672
United Kingdom	Aug 74	-749	-8,066	-2,767	-5,299
Italy	Jun 74	-556	-3,566	-1,307	-2,259
Canada	Jul 74	-25	581	1,231	-650

BASIC BALANCE**
Current and Long-Term-Capital Transactions

	Latest Period		Cumulative (Million US $)		
		Million US $	1973	1972	Change
United States*	74 II	-2,740	-954	-2,164	1,210
Japan	Aug 74	-233	-9,284	-6,020	-3,263
West Germany	Jul 74	288	5,069	1,438	3,631
France	73 IV	-431	-2,471	-369	-2,102
United Kingdom	74 I	84	84	-1,033	1,117
Italy	73 II	-336	639	971	-332
Canada	74 I	-195	-195	-191	-4

OFFICIAL RESERVES

	Latest Month		Billion US $		
	End of	Billion US $	Jun 1970	1 Year Earlier	3 Months Earlier
United States	Jul 74	14.9	14.5	12.9	14.6
Japan	Aug 74	12.9	4.1	15.1	13.2
West Germany	Jul 74	33.5	8.8	34.1	33.8
France	Aug 74	8.5	4.4	11.2	8.1
United Kingdom	Aug 74	6.8	2.8	6.5	6.9
Italy	Jun 74	5.3	4.7	6.0	6.7
Canada	Aug 74	5.9	4.3	5.6	6.2

*Seasonally adjusted.
**Converted into US dollars at current market rates of exchange.

EXPORT PRICES
US $

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Jul 74	0.5	11.7	25.7	14.3
Japan	Jun 74	0.9	17.1	35.1	29.7
West Germany	Jun 74	-2.4	15.0	20.3	31.8
France	May 74	0.6	14.3	19.3	58.1
United Kingdom	Apr 74	5.9	12.5	23.9	109.7
Italy	Apr 74	5.8	13.3	29.4	73.9
Canada	May 74	1.5	14.9	44.1	59.2

EXPORT PRICES
National Currency

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Jul 74	0.5	11.7	25.7	14.3
Japan	Jun 74	2.7	10.2	44.5	30.6
West Germany	Jun 74	0.2	4.7	17.7	13.5
France	May 74	0.7	10.4	29.4	46.8
United Kingdom	Apr 74	3.8	12.6	28.8	57.7
Italy	Apr 74	5.6	13.8	39.8	63.6
Canada	May 74	0.8	12.4	38.2	48.4

IMPORT PRICES
National Currency

	Latest Month	Percent Change from Previous Month	Average Annual Growth Rate Since 1970	1 Year Earlier	3 Months Earlier
United States	Jul 74	2.4	19.5	52.3	27.1
Japan	Jun 74	2.3	17.7	83.2	27.7
West Germany	Jun 74	1.7	6.9	29.7	16.9
France	May 74	4.0	16.0	63.0	74.4
United Kingdom	Apr 74	3.5	21.5	61.6	89.5
Italy	Apr 74	5.4	26.0	90.8	163.4
Canada	May 74	3.4	10.6	30.3	54.2

EXCHANGE RATES Spot Rate
As of 27 Sep 74

	US $ Per Unit	Percent Change from Dec 66	18 Dec 1971	19 Mar 1973	20 Sep 1974
Japan (Yen)	0.0034	21.86	3.54	-11.60	-0.59
West Germany (Deutsche Mark)	0.3765	49.76	21.33	6.53	0.11
France (Franc)	0.2105	4.26	6.91	-4.49	0.86
United Kingdom (Pound Sterling)	2.3330	-16.40	-10.46	-5.20	0.82
Italy (Lira)	0.0015	-5.56	-12.09	-14.58	0.07
Canada (Dollar)	1.0150	10.04	1.72	1.73	0.13

TRADE-WEIGHTED EXCHANGE RATES***
As of 27 Sep 74

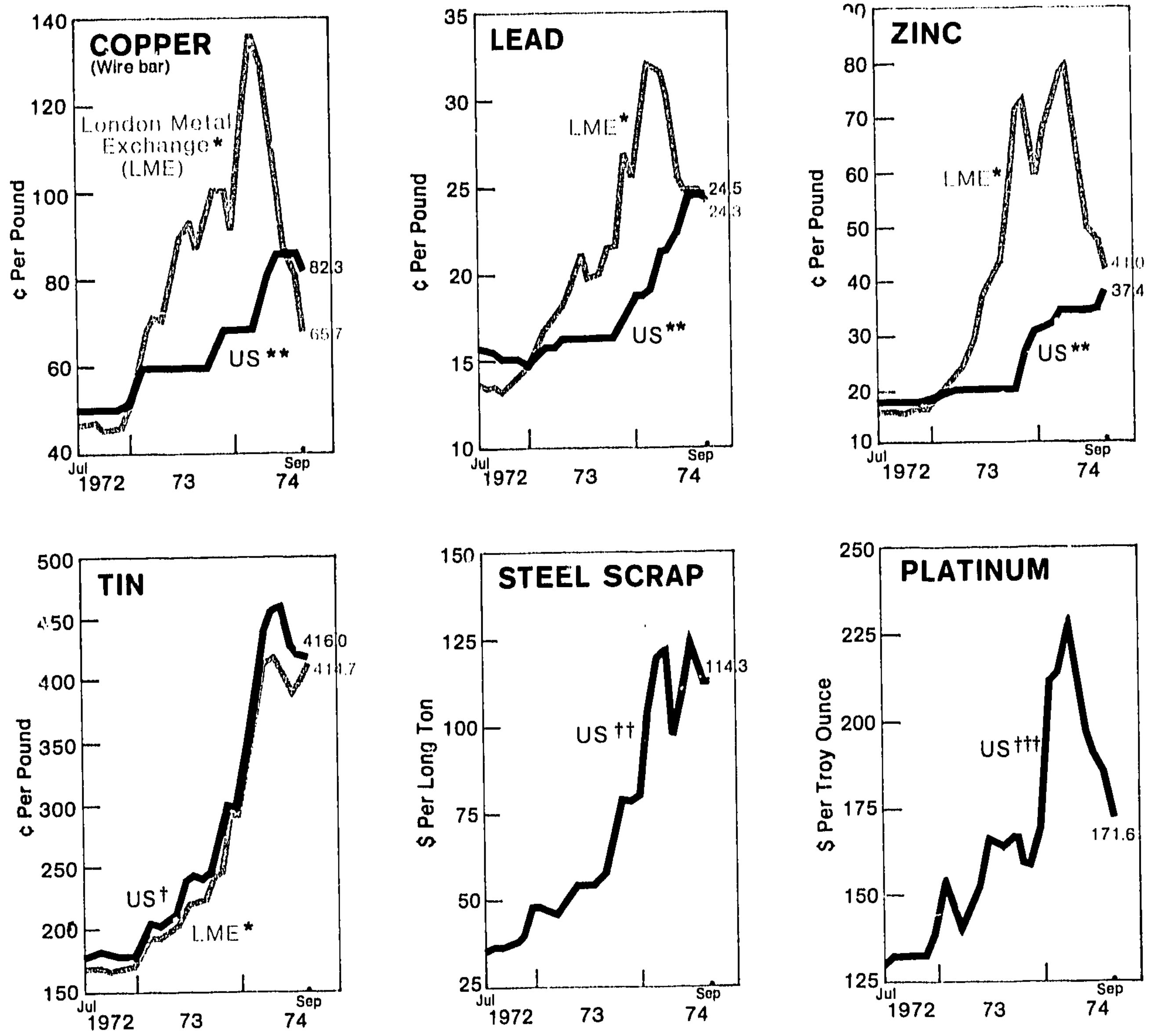
	Percent Change from Dec 66	18 Dec 1971	19 Mar 1973	20 Sep 1974
United States	-13.87	-4.62	1.97	0.26
Japan	13.80	0.25	-11.58	0.71
West Germany	29.12	12.24	7.24	-0.01
France	-15.80	-2.49	-4.95	0.76
United Kingdom	-34.05	-19.90	-5.52	1.41
Italy	-25.70	-24.40	-17.53	-0.09
Canada	7.73	1.14	2.78	0.21

***Weighting is based on each listed country's trade with 16 other industrialized countries to reflect the competitive impact of exchange-rate variations among the major currencies.

2 October 1974

METAL PRICES

(Monthly Average Price)



COMMODITIES

	Cash Prices 30 Sep	Week Ago	Aug 74 Average	Sep 73 Average
Copper-LME (¢ per pound)	68.0	64.4	81.7	87.6
Copper-US (¢ per pound)	79.6	79.6	85.6	59.5
Lead-LME (¢ per pound)	24.8	24.4	24.9	20.1
Lead-US (¢ per pound)	24.5	24.5	24.5	16.5
Zinc-LME (¢ per pound)	41.2	41.9	47.8	44.1
Zinc-US (¢ per pound)	38.0	38.0	35.0	20.3
Tin-LME (¢ per pound)	411.4	418.4	398.0	226.6
Tin-US (¢ per pound)	406.0	412.8	423.0	240.3
Steel scrap ($ per long ton)	115.7	115.5	114.3	58.5
Platinum ($ per troy ounce)	173.5	171.0	185.3	163.7

**Approximates world market price frequently used by major world producers and traders, although only small quantities of these metals are actually traded on the LME.*
***Producers' price, covers most primary metals sold in the United States.*
†Quoted on New York market. ††Composite price for Chicago, Philadelphia, and Pittsburgh. †††New York dealers' price.

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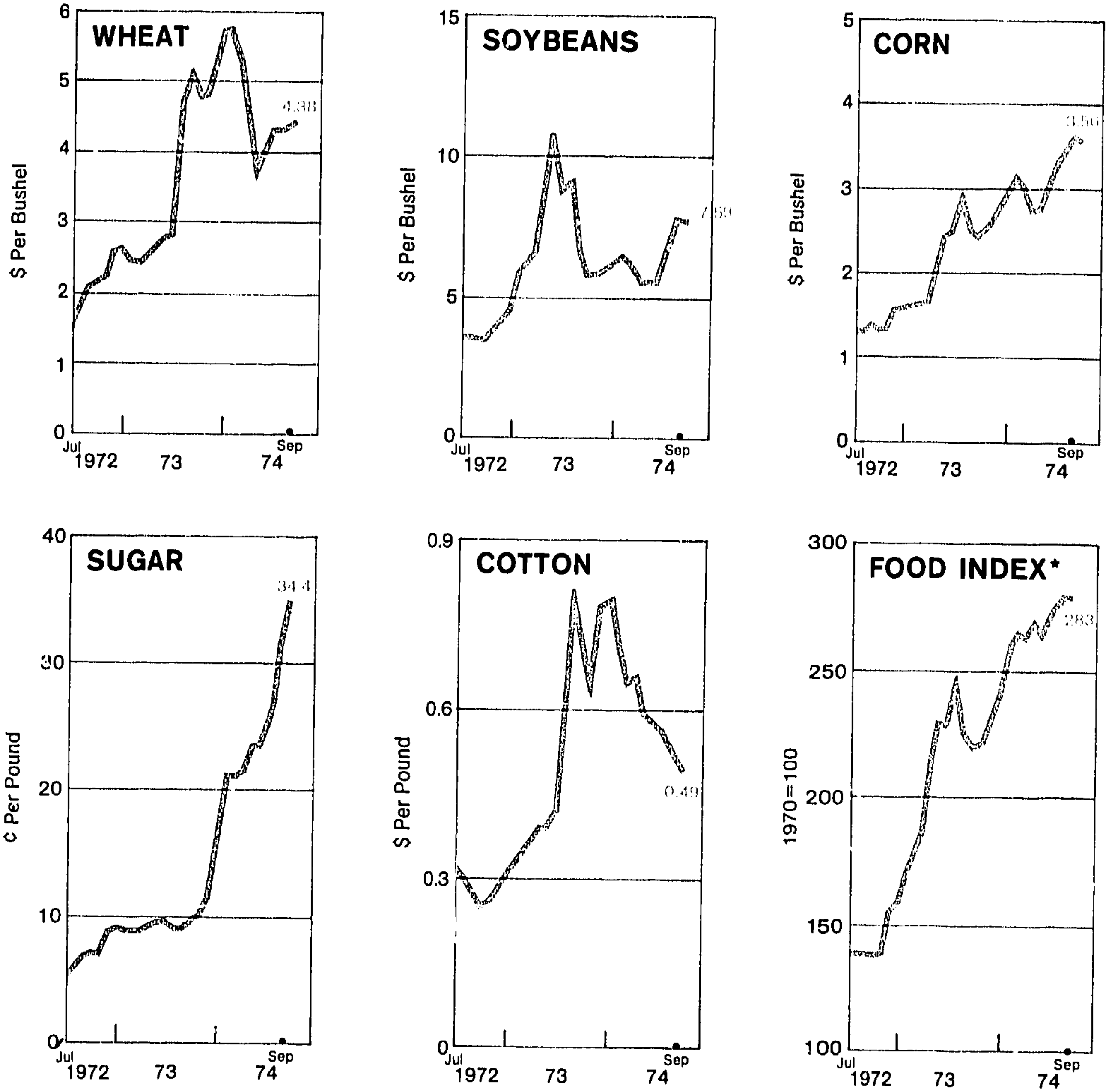
AGRICULTURAL PRICES

(Monthly Average Price)



* This is a compiled index by the Economist for 16 food commodities which enter international trade. Commodities are weighted by 3-year moving averages of imports into industrialized countries.

COMMODITIES

	Cash Prices			
	30 Sep	Week Ago	Aug 74 Average	Sep 73 Average
Wheat–Kansas City #2 Hard Winter ($ per bushel)	4.66	4.37	4.34	5.09
Corn–Chicago #2 Yellow ($ per bushel)	3.97	3.59	3.63	2.47
Soybeans–Chicago #1 Yellow ($ per bushel)	8.63	7.72	7.69	6.50
Sugar–World Raw New York #11 (¢ per pound)	36.50	36.00	31.70	9.00
Cotton–Memphis 1 1/16" ($ per pound)	0.5115	0.4690	0.5120	0.8080

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Annex to

Economic Intelligence Weekly

Developed Countries; Recent Trends in Inflation

STAT

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DEVELOPED COUNTRIES: RECENT TRENDS IN INFLATION

Introduction

1. Inflation currently is viewed as the chief economic problem in almost all developed countries. Price increases began accelerating in mid-1972, gained momentum throughout 1973, and were proceeding at an unprecedented rate by early 1974. By mid-1974, wholesale prices in major OECD countries were on the average 36% above mid-1972 levels, making the price spiral the steepest and most sustained in post-war history. Consumer prices were up 22% on the average. Although the worst of the price rise is probably over, inflation will remain a serious problem in all developed countries through mid-1975, at least.

2. The price spiral has gone through several fairly distinct phases. The initial phase began in 1972, when many governments adopted expansionary monetary policies to spur growth. In that year, the money supply in most major countries increased at least 50% faster than nominal GNP. By mid-1973, commodity prices had risen to record levels and were a prime factor in the continuing inflation. Oil supply disruptions and the huge increase in oil prices last winter added impetus to this second round of inflation, which lasted until mid-1974. More recently, wage-cost push has become the chief stimulus to inflation.

Anatomy of Inflation*

3. From the standpoint of individual countries, price increases in 1972-73 were the result mainly of rising costs for foodstuffs, industrial raw materials other than oil, and imported manufactures. Our analysis indicates that through 1973:

- higher costs for foodstuffs, raw materials, and imported manufactures accounted directly and indirectly for more than half of the wholesale price increase in most major countries;

* To measure the impact of higher input prices on overall prices, we have used input-output tables for the major countries. The influence of higher costs for foodstuffs, raw materials, oil, imports of manufactured goods, and labor was measured by increasing the relevant rows in inverted input-output tables by the amount of the cost increase. In following this procedure, we were assuming that changes in costs are passed through, dollar for dollar.

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- higher labor costs accounted for 10% to 15% of the wholesale price rise in most countries; and

- higher profits contributed appreciably to inflation in almost all major countries because shortages of many products and a general condition of excess demand allowed firms to widen profit margins.

4. Since the start of 1974 the primary causes of inflation have shifted markedly.

- Higher oil costs accounted, directly and indirectly, for roughly half the increase in wholesale prices in the first half of the year.

- Higher labor costs accounted for one-third or more of the price rise in most countries.

- Costs of commodities other than oil played an important, though declining, role.

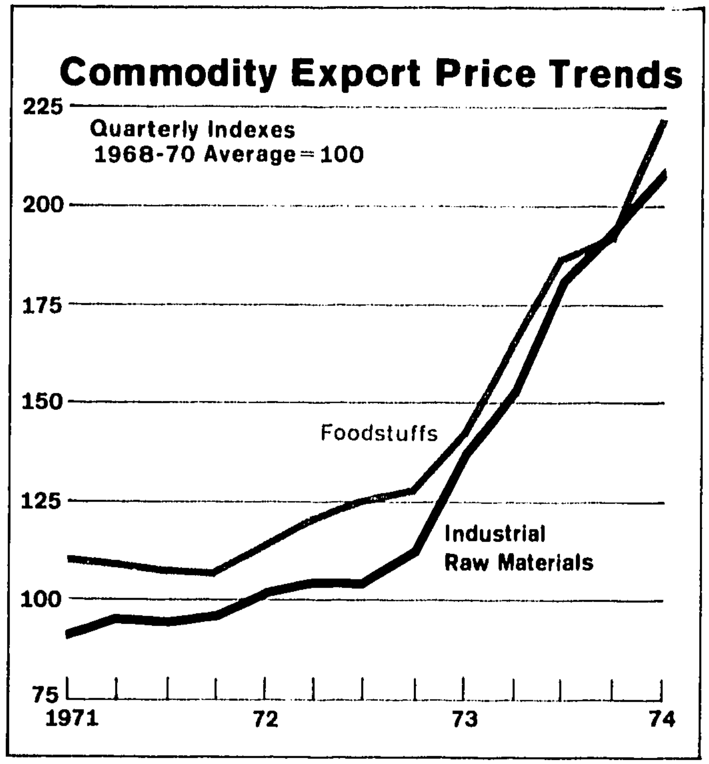
- Profit margins generally declined, reflecting the contractionary impact on aggregate demand of the oil price hike and of anti-inflation measures in certain countries.

Inflation from Mid-1972 to Mid-1974

5. The doubling in commodity prices (see the chart) between mid-1972 and mid-1974 was a global development resulting partly from national decisions to stimulate demand and partly from fortuitous factors that hurt supply. Adoption in early 1972 of expansionary policies – particularly in the monetary field – brought a coincident economic upturn in major countries. The resulting pressure on prices was intensified by poor crops in some countries and by last winter's supply disruptions and enormous rise in oil prices. Under these circumstances, effort by individual governments to control the price spiral could scarcely be effective.

Causes of Increased Commodity Prices

6. Several factors contributed to the rise in commodity prices. One of the most important was crop shortfalls in several countries. In the crop year ending in June 1973, world grain production fell 3%, compared with an average annual increase of 3.5% in 1960-71. Global demand for food, on the other hand, increased more than the usual 4%, largely because of rising demand in Communist countries and the LDCs. Grain output fully recovered last year, but supplies remained tight because global demand continued to accelerate increasingly (by 4.5% during the past year).



7. Unusually strong demand generated substantial price increases for numerous industrial raw materials. Demand rose especially fast last year, when industrial output in the major countries increased 12%–double the long-term average. Capacity constraints prevented a corresponding increase in output of most raw materials. Copper production, for example, rose only 4% last year, compared with the 8% growth in consumption (see Table 1). The resulting inventory drawdowns left commodity markets tight even before the oil crisis hit. Commodity prices then surged further, primarily because of heavy speculative buying to hedge against shortages, continuing price increases, and currency changes. Not until mid-1974, when speculation eased, did raw material prices generally return to pre-crisis levels.

8. The huge increase in oil prices gave inflation another hard push (see Table 2). As a result of the OPEC countries' price hikes since early October 1973, the delivered cost of crude oil for most importing countries has roughly tripled. Countries with substantial crude oil production – the United States and Canada – have been affected much less than those with little or no output. For example,

average crude oil prices in the United States are now 96% above a year ago, while Japan's are up 248%, in terms of yen.

Some Domestic Factors

9. Lack of surplus production capacity in key industries contributed to the price spiral in all major countries. Growth of capacity was slow in the early 1970s owing to the sluggish growth of investment. Investment in plant and equipment rose an average of only 3.8% annually in 1970-72, roughly half the long-term rate. In a few industries, notably steel and synthetic textiles, strong demand quickly produced a sellers' market that enabled firms to increase prices and profit margins.

10. Although investment generally recovered in 1973 (see Table 3), growth in plant capacity apparently has continued below normal. The lag is explained partly by the fact that time is needed to complete investment projects. Another reason, probably more important, is that a growing share of investment is going into equipment to control pollution, which yields little or no increase in production capacity. In the steel industry, for example, an estimated 10% to 15% of fixed investment now is devoted to pollution control. The Japanese have estimated that as much as 12% of total investment last year consisted of pollution-control equipment, possibly tripling the 1970 share.

Current Phase of Inflation

11. Current price pressures in the developed countries are essentially cost-push in nature. Basically the problem is that certain industries and labor are determined to restore their real income, which has been eroded by the redistribution of income to producers of oil and other key commodities. The response from labor has been to substantially increase wage demands. Enterprises are raising prices as circumstances demand or allow. Governments are avoiding wage controls, hoping instead to moderate inflation by constraining aggregate demand. With the slowdown in economic growth, national leaders apparently expect business to resist excessive wage settlements and to absorb a portion of higher labor costs by reducing profit margins.

Labor Costs

12. Wage rates are already increasing sharply (see Table 4). Settlements negotiated in major West European countries during the first half of 1974 averaged

around 20%, roughly 50% above last year. By and large, hourly wage rates during the first half of 1974 kept pace with inflation, but reduced working hours meant a cut in real income. More recent settlements call for pay rates to increase slightly faster than prices are now rising.

13. In contrast to 1973, wage increases this year are not being offset by productivity gains. With output stagnating or declining, the growth in output per man-hour has plummeted over the past six months. A major reason is that firms are reluctant to reduce their work forces in response to difficulties that they hope will be short-lived. As a result, unit labor costs are increasing substantially. In Japan, unit labor costs rose at a 19% annual rate in the first half of 1974, compared with only 3% in 1973 (see Table 5). The increases in most other developed countries are smaller, but still large.

Other Factors

14. Capacity constraints are still putting pressure on prices in some industries. The problem is most evident in basic industries, which are operating near capacity and enjoying good profit margins. Steel prices, for example, have generally risen 30% since the start of 1974, while production costs on the average have risen 20% or less. Profit margins have narrowed for most other industries because weak demand kept prices from increasing as fast as production costs. The profit squeeze is particularly severe in the United Kingdom and Japan.

Prospects for Inflation Rates

15. Inflation will remain a serious problem in all developed countries through mid-1975, and probably beyond that time. We believe that consumer prices in major OECD countries will on the average increase at annual rates of 15% in the second half of 1974 and 13% in the first half of 1975. These rates compare with average annual increases of 3.5% in 1960-71. Wholesale prices are projected to rise by roughly 13% from mid-1974 to mid-1975 – about four times the long-term annual average. The expected increases for consumer and wholesale prices are well below the rates experienced in the first half of 1974.

16. Japan, Italy, and the United Kingdom face the most severe continuing inflation. Higher labor costs alone will boost Japanese wholesale prices by an estimated 11% during the first half of 1975. Consumer prices will rise even faster, as previous cost increases are passed along to final consumers. Growing labor costs

will be the chief cause of Italy's expected 20% rise in wholesale prices and Britain's expected 10% increase. West Germany's inflation rate probably will reach only about 8% because wage settlements have been more moderate than in other European countries.

17. Tight monetary and fiscal policies promise only limited success in curbing inflation. Constraints on aggregate demand can limit price increases only to the extent that business is induced to absorb cost increases. Profit margins in many industries have already been squeezed by the fall-off in demand in the first half of 1974. With costs continuing to rise, many firms will be inclined to reduce output rather than profits. Relaxation of demand-management policies would ease cost pressures by permitting higher production and more rapid productivity gains. If demand increased very much, however, production bottlenecks would surface fairly rapidly in certain industries.

18. Price increases are likely to erode a large part of recent wage hikes. Indeed, in Italy, real wages are expected to decline through mid-1975, and in the United Kingdom real wages will increase only by an estimated 3%. Accelerating wage demands could give considerable stimulus to inflation. In most developed countries, a 5% increase in unit labor costs would boost wholesale prices by about 2%.

19. Crop shortfalls this year threaten another round of exogenous price increases. Prices of most US farm commodities entering international trade have strengthened recently, following several months of decline from record highs. The London ***Economist*** index of prices for 16 internationally traded foodstuffs increased 3% in August alone. Low world stocks, withholding of commodities by farmers, and speculative buying prompted by adverse weather are contributing to the pressure on supplies and prices. Prices of industrial raw materials, on the other hand, are continuing a downward trend.

Table 1

Growth of World Consumption of Selected Industrial Materials

	Percent Increase	
	Average Annual 1967-72	1973
Aluminum	8.1	13.1
Copper	5.4	8.0
Cotton	1.2	2.9
Nickel	1.7	11.6
Tin	0.6	6.7
Zinc	5.2	6.9

Table 2

Developed Countries: Impact of Oil Price Hikes

Percent

	From Oct 1973 to Midyear 1974[1]	
	Increase in Delivered Price of Crude Oil	Increase in Wholesale Prices
France	251	4.5
Italy	212	11.3
Japan	248	8.8
United Kingdom	173	5.2
United States	96	5.1
West Germany	170	6.1

1. In terms of national currency. Data for France, Japan, and the United Kingdom are to June 1974, for Italy to April, for the United States to August, and for West Germany to May.

Table 3

Developed Countries: Growth in Gross Private Fixed Investment[1]

Percent

	Average Annual 1961-70	Average Annual 1971-72	1973
France	9.0	6.7	6.6
Italy	4.9	0.6	12.0
Japan	15.4	4.3	19.3
United Kingdom	5.0	-3.2	12.0
United States	5.1	4.1	12.8
West Germany	7.3	2.3	1.8

1. At constant prices, excluding residential construction.

Table 4

Developed Countries: Increase in Hourly Wage Rates

Percent[1]

	First Half 1972	Second Half 1972	First Half 1973	Second Half 1973	First Half 1974
Canada	5.6	9.9	4.7	9.3	12.3
France	11.1	11.8	14.4	15.4	20.0
Italy	9.7	13.1	24.7	28.9	22.0
Japan	12.5	12.8	21.4	28.4	25.4
United Kingdom	12.3	19.3	6.4	16.8	16.0
West Germany	10.4	6.2	12.4	8.2	14.0

1. At annual rate.

Table 5

Developed Countries: Increase in Unit Labor Costs

Percent[1]

	First Half 1972	Second Half 1972	First Half 1973	Second Half 1973	First Half 1974
Canada	2.8	5.7	1.1	9.6	4.9
France	3.9	5.2	6.1	11.9	16.0
Italy	5.8	0.3	12.2	21.5	17.0
Japan	2.5	2.2	0.4	7.8	19.0
United Kingdom	8.0	10.0	-0.3	14.5	16.0
West Germany	2.5	4.3	3.5	9.7	9.2

1. At annual rate.